SUPREME COURT, U. S.
FILED
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1973

No. ...73-1213

OLIVER R. GRACE, THE GREEN FUND, INC., S. WILLIAM GREEN, EVELYN GREEN and CYNTHIA COLIN, as Executors of the Estate of LOUIS A. GREEN, deceased, EVELYN GREEN and ELBRIDGE SMITH, individually and as stockholders of AMERICAN-HAWAIIAN STEAMSHIP COMPANY in behalf of themselves and of said corporation, and LEVENTRITT LEWITTES & BENDER,

Petitioners,

against

DANIEL K. LUDWIG, BERKSHIRE INDUSTRIES, INC., AMERICAN-HAWAIIAN STEAMSHIP COMPANY, TRUDE WEININGER, PREMIER INVESTING CORPORATION and ROBERT KORSEN,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

Petitioners pray that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Second Circuit, entered in the above-entitled case on September 12, 1973, rehearing denied November 14, 1973. Petitioners were plaintiffs and respondents were defendants below.

Opinion Below

The Opinion of the Court of Appeals is reported in 484 F2d 1262. A copy is appended to this petition as Appendix A (1a et seq.). The District Court did not render any opinion but its reasons as stated in open court are set forth in Appendix C hereto (13a).

Jurisdiction

The judgment of the Court of Appeals was dated and entered on September 12, 1973 and the Orders denying the duly filed Petition For Rehearing, with suggestion that it be in banc, on November 14, 1973. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254.

Statute Involved

Section 17 of the Investment Company Act of 1940, 15 U.S.C. § 80a-17, is quoted in pertinent part at 2a, footnote 1.

Questions Presented

1. Where minority stockholder attorneys concededly prevented a fraudulent merger of their corporation, a registered investment company, in a proceeding before the Securities and Exchange Commission (SEC) under § 17 of the Investment Company Act, inducing the parent-applicant to admit that the investment company's stock, as to which it had originally offered $275 a share in the proceeding, was worth $650, a 73 million dollar increase in the company's value, did not the courts below err in dismissing, "for failure to state a cause of action", a complaint which seeks to have the investment company reimburse said minority stockholders for the fees they personally paid to those attorneys for those services, in the light of (a) *Mills* v. *Electric Auto-Lite Co.*, 396 U.S.

375, which requires reimbursement and award of attorneys' fees for significant private enforcement of the securities laws, for benefits conferred, and to avoid unjust enrichment, (b) the stated position of the SEC that interested persons should be encouraged to participate in §17 Commission proceedings as "essential for effectuation of the policies of the Act", and (c) the "net effect" of the Opinion below as noted and disapproved by the SEC—"to by-pass the Commission and to wage the battle of the fairness of the transaction in district court, rather than before the Commission, which is the forum established by Congress for the determination of such questions"?

2. Did not the complaint also state a valid cause of action for an award to the minority stochkolders' attorneys for those services, payable by the investment company or the other minority stockholders or both?

3. Were the investment company's parent-applicant and the latter's sole, dominating stockholder not, also, liable for such reimbursement and award, because they were guilty of fraud and harassment in the SEC proceeding?

Statement of the Case

A. Nature of Present Action, Federal Question Jurisdiction, and Parties.

This is an action filed in the United States District Court for reimbursement and award of attorneys' fees, in federal equity and under the federal securities laws. The claims grew out of the plaintiffs' prevention of a fraudulent merger of their corporation, a registered investment company, in a proceeding before the SEC under § 17 of the Investment Company Act and their inducing the parent-applicant to admit that the investment company's stock, as to which it had originally offered $275 per share in the proceeding, was worth $650. This represented a 73 million dollar increase in the company's value.

The District Court's jurisdiction is based on 28 U.S.C. § 1331: the amount of principal in controversy exceeds $10,000 and the action "arises under the . . . laws . . . of the United States." The laws are the federal securities laws; and attorneys' fees for enforcement thereof are "a remedial incident" of such enforceemnt. Hence an action for them is, as was held by the Court of Appeals below, "properly brought in the federal court" (5a).

The parties are as follows:

Plaintiff Leventritt Lewittes Bender ("LLB") is a law firm whose members are duly admitted to practice in this Court. The other plaintiffs were, at material times, minority stockholders of defendant American-Hawaiian Steamship Company ("American-Hawaiian"), owning about 2.5% of its outstanding stock and the only public stockholders actively represented at the SEC hearings.

At material times defendant American-Hawaiian was a registered investment company, controlled and dominated, and with about 91% of its stock owned, by defendant Berkshire Industries, Inc. ("Berkshire"), which is wholly owned, controlled, and dominated by defendant Daniel K. Ludwig ("Ludwig").

The remaining defendants were minority stockholders of American-Hawaiian, owning about 3.5% of its outstanding stock.*

B. The Respective Plaintiffs' Claims.

(I) For the benefits conferred on American-Hawaiian, in increasing its admitted value by $73,000,000 and preserving it as a separate entity:

(1) The plaintiff minority stockholders seek reimbursement from American-Hawaiian of the $408,114 they per-

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* Other minority stockholders, with smaller holdings, owned the remaining 3%.

sonally paid to LLB in fees for LLB's participation in the SEC proceeding.*

(2) LLB, the plaintiff attorneys, seek a reasonable award from American-Hawaiian for their taking the "laboring oar" in thus enforcing the securities laws in the proceeding under § 17 of the Investment Company Act.**

(3) The plaintiffs also claim that Berkshire and Ludwig are liable for those amounts because they were guilty of fraud and harassment in the SEC proceeding.

(II) In the alternative, for the cash benefit of $2,327,000 conferred on defendant minority stockholders by reason of LLB's services in the SEC proceeding, LLB seeks a reasonable attorneys fee from them to prevent their unjust enrichment.

C. The Proceeding Under § 17 of the Investment Company Act.

Berkshire filed its 17(b) application on July 31, 1967, proposing, pursuant to the then § 14:12-10 of the New Jersey General Corporation Law, a short form merger of American-Hawaiian into Berkshire, by resolution of Berkshire's board of directors setting forth the terms of the merger. Minority stockholders of American-Hawaiian could either accept the price fixed in the resolution or demand an appraisal of their stock. However, Berkshire could not effect the merger without first obtaining SEC approval on a showing that the merger was on terms fair to the minority, did not involve overreaching, and was

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* They also sought repayment of other out-of-pocket expenses of about $54,000. American-Hawaiian, without prejudice to the position of the parties, reimbursed those after commencement of the action.

** The amount was not in isue on the appeal. In LLB's motion for summary judgment which the District Court deferred, the request was for $10,000,000, approximately 14%.

consistent with the policies of the Act. In its application to the SEC, Berkshire estimated the net value of American-Hawaiian at about $53 million and proposed to offer $275 per share to American-Hawaiian minority stockholders.

The parties to the SEC proceeding were Berkshire and the SEC's Division of Corporate Regulation (Rule 9(a), SEC Rules of Practice, 17 C.F.R. § 201.9(a)). The SEC on October 25, 1967 directed a hearing on notice to all interested parties. Grace and the other plaintiff stockholders thereupon retained LLB who appeared for them after leave to participate had been granted pursuant to Rule 9(c), 17 C.F.R. § 201.9(c). Evidentiary hearings on Berkshire's application were conducted before a hearing examiner of the SEC from January 4th to June 7th, 1968, totalling about 50 hearing days. Counsel for the SEC's Division of Corporate Regulation also appeared. Seventeen witnesses testified, 550 exhibits were introduced and a 7500 page transcript of the hearing was compiled. At the end of the hearings the parties agreed pursuant to Rules 8(b) and (c), 17 C.F.R. § 201.8(b) and (c), to waive an initial decision by the hearing examiner and to permit the SEC staff to assist the Commission in the preparation of its decision. After receiving extensive briefs and proposed findings from LLB and Berkshire, only, the full Commission heard oral argument by them on November 12, 1968.

Prior to any decision by the Commission, Berkshire advised the SEC that a sale of certain property owned by American-Hawaiian might have an impact on the valuation of the American-Hawaiian stock. Berkshire thereafter applied for and was granted on June 12, 1969 a re-opening of the proceedings to adduce additional evidence. After two days of hearings (August 4 and 11, 1969) a settlement proposal of Berkshire was rejected by LLB and Berkshire sought leave to withdraw its 17(b) application. The SEC on November 28th, 1969 allowed the withdrawal and denied LLB's claim for a fee to be paid by American-Hawaiian

or Berkshire, without prejudice to any other legal remedy which the plaintiffs might pursue, since the agency lacked jurisdiction to award counsel fees.

D. LLB's Contribution.

The District Court assumed the truth of the facts alleged in the complaint and the supporting papers (4a). These showed in substance as follows:

LLB, through Mr. Bender, took the laboring oar in the proceeding before the SEC and was recognized in fact as the class representative by the hearing examiner. Mr. Bender took the lead in cross-examining opposing experts; found, prepared, and put on two of his own experts; argued twice orally before the full Commission; and submitted to the Commission elaborate briefs and proposed findings. The SEC staff offered no experts and submitted no briefs or findings. Mr. Bender opposed Berkshire's successive offers as inadequate and pointed to evidence that its applications and presentations to the SEC were tainted with fraudulent representations.

As the result very largely of LLB's efforts, Berkshire successively raised its original offer of $275 to $375 per share at the end of applicant's case, $575 per share at the end of participant's (Mr. Bender's) case and applicant's rebuttal, and $650 per share prior to the reopened hearings in August, 1969.

At the August 4, 1969 session referred to above, the hearing examiner granted an adjournment for discussion between "the applicant and the participant"; viz. Mr. Bender. In the ensuing conferences between Berkshire's attorneys, and LLB, Berkshire refused to negotiate a settlement offer higher than $650 or to prove its fairness to the SEC without Mr. Bender's prior commitment to accept that figure; after consultation with plaintiff stockholders, he refused to approve $650. As a result of that opposition by

LLB, Berkshire decided to and did drop the proposed merger. LLB thus thwarted the fraudulent merger.

Thereafter, American-Hawaiian informed its stockholders that it planned to apply to the SEC for deregistration as an investment company under § 8(f) of the Investment Company Act (15 USCA § 80-a8(f)). But that section provides as follows: "If necessary for the protection of investors, an order under this subsection may be made upon appropriate conditions" to protect the minority.

Subsequently, American-Hawaiian counsel entered into a negotiation with LLB, representing plaintiff stockholders,* the outcome of which was an undertaking by American-Hawaiian, *inter alia*, not to merge with Berkshire and to call for tenders once a year at a fair price to be passed on by an independent director and in some instances by arbitration; and the SEC then granted an application to deregister American-Hawaiian as an investment company, making continued compliance with the undertaking a condition of the order of deregistration.

Pursuant to the call for tenders, defendants Weininger and Premier Investing Corporation in 1972 settled with Berkshire at $600 a share. In August 1973 defendant Korsen and the plaintiff stockholders sold their shares to Berkshire at $725 per share.**

Thus, failing to get the exemption from the SEC, because of LLB's vigorous opposition, Berkshire was prohibited from going through with the merger. American-Hawaiian continued as a separate going concern and corporate entity, worth, on Berkshire's own admission, 73

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* For which no fee is sought herein from defendants.

** In September 1973 LLB received $253,800 (in addition to the amount of $154,314 previously paid) from certain plaintiffs pursuant to their agreement on sale of their shares at $725 per share; of the total amount paid LLB, approximately $29,000 ($13 per hour) was non-contingent and the balance was contingent.

million dollars more than the original application recognized.

The District Judge summarized what he accepted as the facts for the purpose of ruling on the motion to dismiss, as follows:

> ". . . plaintiff's [sic] attorney . . . in fact did the work which produced that result . . . by being the laboring oar . . ." (App. in appeal to Court of Appeals, 100A-101A)
>
> "As a factual matter, [LLB] is a representative of the class . . ." (*id.* 102A)
>
> "if you [LLB] hadn't come in there it would have been a fiasco and the corporation would have lost the $73,000,000 . . ." (*id.* 107A)

E. Disposition Below and the Stated SEC Position.

The lower court dismissed the complaint, on motion for judgment on the pleadings, "for failure to state a cause of action".

The major premise of the Court of Appeals' Opinion, affirming, is that *Mills* v. *Electric Auto-Lite Co.*, 396 U.S. 375, is to be distinguished on the ground that the need to encourage private enforcement of the securities laws applies to proceedings in court but not to procedings before the SEC (6a-7a); in the latter the SEC staff takes an active part and

> "A precedent here would encourage intervention in comparable cases . . . before the SEC . . . The introduction of additional cooks might not only spoil the broth but paralyze the chef." (10a)

After the decision below, the SEC in a communication to the Court of Appeals expressed serious objection to this policy determination of the court, stating in part as fol-

lows:

> "The Commission welcomes the participation of responsible persons in its administrative proceedings. The Commission does not share the Court's fear that 'additional cooks might . . . spoil the broth' and is confident that it could deal with 'competition and maneuvering among counsel.' . . . (20a)
>
> * * *
>
> "In applications under Section 17(b) of the Investment Company Act, . . . the evidence supporting the application is of necessity one-sided, and the Commission's staff does not and cannot conduct a full-scale investigation of the merits of applications, except in those relatively rare instances where the application appears to require such.
>
> "If an interested person has information tending to show that the proposed transaction does not in fact comply with the statutory standards, it is esential for effectuation of the policies of the Act that that person bring his views to the Commission's attention. We believe that the effect of the paragraph in the Court's opinion beginning at page [10a] could be to discourage the participation of interested persons in Commission proceedings and therefore, in the Section 17(b) context, for example, to deprive the Commission of the knowledge of interested persons other than the applicant." (21a-22a)

The SEC took specific objection to the final paragraph of the Court of Appeals' Opinion (10a), which summarized the major premise and policy determination pervading the Court's entire Opinion and decision. The Court of Appeals answered the SEC in part as follows:

> "We do not deem it appropriate at this late date to accede to the Commission's request to delete a paragraph of the opinion because of some apprehension

that it may possibly discourage participation in some future proceedings." (24a)

But in that final paragraph of its Opinion, the Court had stated that an award "here would encourage intervention in comparable cases . . . before the SEC . . ." (10a)—thus, its decision was intended to discourage such intervention, as the SEC apprehended.*

Reasons for Granting the Writ

The decision below creates an unwarranted exception to *Mills* v. *Electric Auto-lite Co.*, 396 U.S. 375. The Court of Appeals lays down a policy for the SEC in a matter of great importance to effective enforcement of the securities laws, in conflict with the policy recommended and desired by the SEC, the agency charged by Congress with primary responsibility for administration of the securities laws. The decision below, unless reversed, will seriously discourage prompt and efficient public-private enforcement of the securities laws.

A. The rule established by *Mills* is that private enforcement of the securities laws "provides a necessary supplement to Commission action" (at 382) and therefore should be encouraged by the reimbursement and award of attorneys' fees for such services. The Court of Appeals holds, however, that this rule should not apply to private

* Appendix E hereto (§ 15a *et seq.*) reproduces in full the SEC communication to the Court of Appeals and that court's reply, as well as the earlier exchange of correspondence between them. The SEC stated that it "takes no position with respect to the result reached by the Court in this case" (19a). The necessary consequence, however, of the SEC's policy position is disagreement with the result reached by the Court of Appeals in this case.

enforcement in proceedings before the SEC because its staff is active in such proceedings and "additional cooks might not only spoil the broth but paralyze the chef" (10a). The SEC, however, "does not share" the Court of Appeals' "fears". Its position is, on the contrary, that it "welcomes the participation of responsible persons in its administrative proceedings"; that in section 17 proceedings, "the evidence supporting the application is of necessity one-sided"; that except in "rare instances" the "staff does not and cannot conduct a full-scale investigation"; and that minority participation in the proceedings before the SEC "is essential for effectuation of the policies of the Act" (20a-22a).

Thus, the policy of encouraging private enforcement of the securities laws as "a necessary supplement to Commission action", by the reimbursement and award of an attorney's fee, applies to such services whether in court or before the SEC. The Court of Appeals' attempted distinction between private enforcement in Court and private enforcement in an SEC proceeding is based on a misapprehension of the functions and capabilities of the SEC staff in Section 17 proceedings, generally,* and in disregard of the express position of the SEC that private participation in Section 17 proceedings should be encouraged as "essential for effectuation of the policies of the Act."

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* The decision assumes, without any foundation, that the function of the SEC staff was the same as that performed by the plaintiff stockholder attorneys; *viz.* to advocate the highest price supportable by the facts. The SEC does not view its staff's function in that light at all. Thus, the decision overlooks the decisive facts that (although the SEC staff was present througout the hearings), the SEC staff, unlike the stockholder attorneys, took no position in opposition to the applications, produced no witnesses, did not provide the main cross-examination of applicant's witnesses, filed no briefs or proposed findings of fact, and presented no oral argument on the merits. In fact the SEC staff exercised a quasi-judicial and limited questioning function and not the advocate's function which vigorous enforcement of the securities laws demands.

The basic issue is, simply, whether private participation in Section 17 proceedings is "a necessary supplement to Commission action". The Court of Appeals says "No", but the SEC, which is in a better position to know its own necessities, says "Yes". We believe the Supreme Court should review this question, of fundamental importance for SEC proceedings enforcing the securities laws.

The lower courts recognized, for purposes of passing on the defendants' motion, that it was plaintiffs who, with the permission of the hearing examiner, took the laboring oar and were primarily responsible for getting Berkshire to increase the price from $275 to $650, and for thwarting a fraudulent merger. Therefore, the inquiry of what the SEC might have done absent LLB is irrelevant, immaterial and speculative. The test of what the SEC might have done (but didn't) has as its purpose and effect the discouragement of private participation in SEC proceedings.

The Court of Appeals states "A precedent here would encourage intervention in comparable cases . . ." (10a). We respectfully ask, where intervention prevents a fraudulent merger and produces an increase in price from $275 to $650 per share, what best carries out Congressional purpose—"to encourage" or "kill off" that kind of intervention?

B. The Court of Appeals states (8a):

> "Had the SEC granted the exemption and the initial $275 offer been approved and had LLB then successfully appeared in a derivative action on behalf of the public stockholders, we would have a decidedly different situation."

The SEC makes the following pertinent comment thereon (23a):

> "The 'policy considerations' alluded to by the Court at [10a] of its opinion could be read to indicate that,

> so long as the Commission's role in Section 17(b) proceedings is more than 'perfunctory', under no circumstances may a participant be compensated for his counsel fees and expenses. If this is so, then a person with knowledge of facts indicating that a Section 17 application should not be granted will be encouraged to sit out the administrative proceeding and, if the Commission approves the application, to make a collateral attack upon the transaction in district court alleging that the Commission was defrauded. In the collateral action, counsel would probably be entitled to reimbursement of counsel fees, as the Court suggests in its opinion [at 8a]. The net effect, then, would be to by-pass the Commission and to wage the battle of the fairness of the transaction in district court, rather than before the Commission, which is the forum established by Congress for the determination of such questions."

Thus, the Court of Appeals, by discouraging private participation in proceedings before the SEC, encourages displacement of the SEC by the district court as the primary tribunal for challenges to the fraudulence of applications, in disregard of the statutory policy.

Furthermore, the holding is directly contrary to the Second Circuit's own holding in *Blau* v. *Rayette Faberge, Inc.*, 389 F2d 469, 472, that it " 'would be penalizing efficiency and expediency' " to reward a stockholder for reimbursement of his attorney's fees only when court litigation is brought but to deny such reimbursement entirely where the same benefit results without the necessity of such proceedings.

C. The SEC noted (22a) that although it could grant a fee, as a condition of approving a modified Section 17 application, to "a participant who had taken a substantial role in bringing the fact of unfairness [in an application preceding the ultimate one] to the Commission's atten-

tion", the Commission has no jurisdiction to reward such service where the application is finally withdrawn. The federal courts do, however, have such jurisdiction (5a).

Given, as the SEC urges, that encouragement of private participation in the proceeding before the Commission "is essential for effectuation of the policies of the Act", it follows that the award should not depend on whether the application is modified and approved or is withdrawn. The service consists in taking "a substantial role in bringing the fact of unfairness" in an application "to the Commission's attention" (22a). That service is performed, equally, where it results in withdrawal of the application or where it results in a modification which is then approved as fair.

Furthermore, if the grant is made to turn on whether an application is ultimately granted as modified or whether it is withdrawn, interested persons will still be induced thereby "to by-pass the Commission and to wage the battle . . . in district court", because the service in court will be rewarded under *Mills*—thereby frustrating Congressional policy on prompt enforcement before the SEC (23a). Alternatively, lawyers will be encouraged to accept cheap settlements while the proceeding is pending before the SEC as a means of obtaining some legal fee, thereby encouraging collusion with the applicant and lowering the standards of the bar in enforcement of the securities laws.

The Court of Appeals held that the thwarting of a fraudulent merger of an investment company into its controlling corporation does not constitute a benefit to the investment company and its minority stockholders. The decision thus imposes a requirement that a fraudulent merger be consummated before there can be deemed to be a benefit, another way of saying to the private bar, "stay out of the SEC proceeding, and wait until the case gets to court." That holding is also contrary to well established legal and equitable principles: isn't getting an injunction against violation a benefit?

The decision below loses sight of the fact that under *Mills* (at 392), enforcement of the securities laws constitutes a compensable benefit to the corporation and its stockholders.

Also, contrary to *Mills* which held that the "benefit conferred is capable of expression in monetary terms, if only by estimating the increase in market value of the shares" (at 395), the Court of Appeals held that an increase in the bid price by Berkshire from $275 per share to $650 per share was not an increase in market value and therefore of no benefit to the corporation and to its stockholders. This holding is clearly erroneous since the bid price of $650 per share is an admission against Berkshire's interest and indicates that the market value is at least that amount. In fact Berkshire subsequently paid $725 per share.

The decision below encourages the bulk of minority stockholders to sit on the sidelines, yet obtain the benefits as here (for example, defendants Weininger and Premier subsequently sold at $600 per share and realized over $2,000,000 and defendant Korsen has now sold to Berkshire at $725 per share and realized a profit of $327,000), without paying a just fee for those benefits. That such stockholders are not obligated to pay any fee to plaintiffs LLB is discriminatory against plaintiff-stockholders who carried the battle and were the only stockholders who were required to pay a fee of $408,000 to plaintiffs LLB, even though all the other stockholders received the benefit bestowed (See *Mills*, at 392).

The decision is contrary to *Mills* which held that legal fees should be paid to the class representative, "through an award against the corporation" (at 395), in order to prevent others from being enriched unjustly at the plaintiffs' expense. *id.*, 392.

Contrary to established principles of equity, the decision permits the wrongdoers, to wit, Berkshire and Ludwig, to pierce the corporate veil for their own benefit. The decision says, in substance (8a), that Ludwig and Berkshire

obtained no benefit by reason of the price increases for their 91% interest, because at all times *they* knew about their fraud and did not deceive *themselves!* The Court of Appeals erroneously focused on the no-benefit to Ludwig and Berkshire instead of on the benefit to American-Hawaiian and its minority. Ludwig and Berkshire are thus able to use their own fraud as a sword for denying any benefit to the corporation. That rationale encourages majority stockholders to defraud the corporation and its minority. The courts do not, in this connection, pierce the corporate veil to distinguish between the respective interests in the corporation of the wrongdoer and of the outside stockholders, e.g. *Angoff* v. *Goldfine,* 270 F.2d 185 (C.A.1).

D. The decision overlooks the critical fact that the fraudulent application that commenced the entire two year proceeding was caused to be filed by Ludwig and filed by Berkshire. The Court instead treats that fact pattern by the erroneous characterization that "the administrative proceeding here was prompted by the statute" (9a). We submit that the statute assumed an honest application, whereas the administrative proceeding here was commenced by a concededly *fraudulent* application, and there was continuing fraudulent conduct throughout the hearing. Not only was the $275 offer fraudulent, but so were the offers of $375, $575 and $650; plaintiffs are entitled to attorneys' fees from Berkshire and Ludwig because they were "forced to litigate" before the SEC "by reason of the vexatious, wanton conduct of a defendant" (9a); *viz.* Berkshire and Ludwig.

E. The Court of Appeals denies plaintiffs procedural due process, in that it does not give them leave to amend their pleadings to allege that the SEC would not have accomplished the result achieved by LLB,* even though its decision de-

* Contra the decision below, the record does permit an inference that the SEC would not have accomplished the result achieved by LLB (App. in appeal to Court of Appeals, 32A-35A, 37A-38A).

parts from the District Court's assumption in passing on the motion that the outcome of the SEC proceeding without LLB would have been a "fiasco" and American-Hawaiian would have lost $73,000,000.

CONCLUSION

For the foregoing reasons, this petition for a writ of certiorari should be granted.

Dated: New York, New York, February 6, 1974.

Respectfully submitted,

SIDNEY BENDER
Pro Se and Attorney for the other Petitioners

Of Counsel:
AARON LEWITTES

APPENDIX A—Opinion of Court of Appeals Dated and Entered Sept. 12, 1973 Affirming Dismissal of Complaint.

Oliver R. GRACE et al., Plaintiffs-Appellants,

v.

Daniel K. LUDWIG et al., Defendants-Appellees.

No. 859, Docket 73-1212.

United States Court of Appeals, Second Circuit.

Argued June 5, 1973.

Decided Sept. 12, 1973.

Action by counsel for some of minority stockholders of subsidiary corporation against subsidiary, parent, parent's sole shareholder and other minority shareholders of subsidiary to recover attorney's fees and expenses arising out of SEC proceeding on application by parent corporation for an exemption which would permit it to absorb subsidiary corporation by short form merger. The United States District Court for the Southern District of New York, Whitman Knapp, J., dismissed suit, and plaintiffs appealed. The Court of Appeals, Mulligan, Circuit Judge, held that such action, in which plaintiffs charged that parent corporation and sole shareholder in proposing price for subsidiary stock engaged in a fraudulent scheme to freeze out public stockholders and to eliminate subsidiary as an independent entity, arose under substantive sections of investment company act and securities exchange act so as to give federal court federal question jurisdiction, and that such attorneys were not entitled to recover attorney's fees and expenses under circumstances.

Affirmed.

1. Courts ⇐289(6)

Action by counsel for minority stockholders of subsidiary corporation to recover attorney's fees and expenses plaintiff charged that parent and defendant sole shareholder in proposing price for subsidiary stock engaged in a fraudulent scheme to freeze out public stockholders and to eliminate subsidiary as an independent entity, arose under substantive sections of investment company act and securities exchange act so as to give federal court question jurisdiction, even as to minority shareholder defendants who, though they did not violate such substantive sections, allegedly benefited from plaintiffs' representation. Securities Exchange Act of 1934, §§ 16(b), 27, 15 U.S.C.A. §§ 78p(b), 78aa; Investment Company Act of 1934, § 44, 15 U.S.C.A. § 80a-43; 28 U.S.C.A. § 1331.

2. Costs ⇐172
Damages ⇐71

Generally, a successful litigant is not permitted to recover his attorney's fees as damages or as reimbursable costs.

3. Costs ⇐172

In special circumstances a court of equity has inherent power to reimburse a successful suitor for costs of litigation, including his attorney's fees.

4. Securities Regulation ⇐217

Attorneys for some of minority stockholders of defendant subsidiary, who represented such stockholders at SEC proceeding on application by defendant parent for an exemption permitting it to absorb subsidiary by a short form merger, were not entitled to recover attorney's fees and expenses, where record did not warrant inference that but for counsel's intervention SEC would have approved allegedly unconscionably low initial offer of parent and, assuming that counsel did pull "laboring oar" in proceedings before SEC, it was basis for a not insignificant fee, and where SEC proceeding was terminated by withdrawal of the application, with result that counsel established no viola-

parts from the District Court's assumption in passing on the motion that the outcome of the SEC proceeding without LLB would have been a "fiasco" and American-Hawaiian would have lost $73,000,000.

CONCLUSION

For the foregoing reasons, this petition for a writ of certiorari should be granted.

Dated: New York, New York, February 6, 1974.

Respectfully submitted,

SIDNEY BENDER
Pro Se and Attorney for the other Petitioners

Of Counsel:
AARON LEWITTES

Oliver R. GRACE et al., Plaintiffs-Appellants,

v.

Daniel K. LUDWIG et al., Defendants-Appellees.

No. 859, Docket 73-1212.

United States Court of Appeals, Second Circuit.

Argued June 5, 1973.

Decided Sept. 12, 1973.

Action by counsel for some of minority stockholders of subsidiary corporation against subsidiary, parent, parent's sole shareholder and other minority shareholders of subsidiary to recover attorney's fees and expenses arising out of SEC proceeding on application by parent corporation for an exemption which would permit it to absorb subsidiary corporation by short form merger. The United States District Court for the Southern District of New York, Whitman Knapp, J., dismissed suit, and plaintiffs appealed. The Court of Appeals, Mulligan, Circuit Judge, held that such action, in which plaintiffs charged that parent corporation and sole shareholder in proposing price for subsidiary stock engaged in a fraudulent scheme to freeze out public stockholders and to eliminate subsidiary as an independent entity, arose under substantive sections of investment company act and securities exchange act so as to give federal court federal question jurisdiction, and that such attorneys were not entitled to recover attorney's fees and expenses under circumstances.

Affirmed.

1. Courts ⇐289(6)

Action by counsel for minority stockholders of subsidiary corporation to recover attorney's fees and expenses arising out of SEC proceeding on application by defendant parent for an exemption permitting it to absorb subsidiary by short form merger, in which defendant sole shareholder in proposing price for subsidiary stock engaged in a fraudulent scheme to freeze out public stockholders and to eliminate subsidiary as an independent entity, arose under substantive sections of investment company act and securities exchange act so as to give federal court question jurisdiction, even as to minority shareholder defendants who, though they did not violate such substantive sections, allegedly benefited from plaintiffs' representation. Securities Exchange Act of 1934, §§ 16(b), 27, 15 U.S.C.A. §§ 78p(b), 78aa; Investment Company Act of 1934, § 44, 15 U.S.C.A. § 80a-43; 28 U.S.C.A. § 1331.

2. Costs ⇐172
Damages ⇐71

Generally, a successful litigant is not permitted to recover his attorney's fees as damages or as reimbursable costs.

3. Costs ⇐172

In special circumstances a court of equity has inherent power to reimburse a successful suitor for costs of litigation, including his attorney's fees.

4. Securities Regulation ⇐217

Attorneys for some of minority stockholders of defendant subsidiary, who represented such stockholders at SEC proceeding on application by defendant parent for an exemption permitting it to absorb subsidiary by a short form merger, were not entitled to recover attorney's fees and expenses, where record did not warrant inference that but for counsel's intervention SEC would have approved allegedly unconscionably low initial offer of parent and, assuming that counsel did pull "laboring oar" in proceedings before SEC, it was basis for a not insignificant fee, and where SEC proceeding was terminated by withdrawal of the application, with result that counsel established no violation of securities act and created no fund for benefit of minority stockholders. Investment Company Act of 1940, § 17, 15 U.S.C.A. § 80a-17.

Appendix A.

5. Costs ⇐172

Failure to establish a fund or to appear for class does not automatically bar a recovery of attorney's fees.

Sidney Bender, New York City (Leventritt, Lewittes & Bender, New York City, of counsel), pro se and for all other plaintiffs-appellants.

William E. Haudek, New York City (Pomerantz, Levy, Haudek & Block, New York City, Abraham L. Pomerantz and Julius Levy, New York City, of counsel), for defendants-appellees Daniel K. Ludwig, Berkshire Industries, Inc., and American Hawaiian Steamship Co.

Charles A. Stillman, New York City (Morrison, Paul, Stillman & Beiley, New York City, and Peter H. Morrison, Benjamin Zelermyer and Julian W. Friedman, New York City, of counsel), for defendant-appellee Robert Korsen.

Gary J. Greenberg, New York City (Stroock & Stroock & Lavan, New York City, of counsel), for defendants-appellees Trude Weininger and Premier Investing Corp.

Before HAYS, MANSFIELD MULLIGAN, Circuit Judges.

MULLIGAN, Circuit Judge:

The controversy before us on originated when the defendant shire Industries, Inc. ("Berkshire" plied to the SEC for an exemption Section 17 of the Investment Co Act of 1940 (the "Act"), 15 U.S 80a–17,[1] which would permit it to its 91% owned subsidiary the defe American-Hawaiian Steamship Co ("American") by a short form m American is a registered closed-e vestment company and the Act pro such merger unless the SEC finds the transaction is reasonable, fair of overreaching and consistent wit general purposes of the Act. Und terms of the proposed merger, A can's minority stockholders were paid cash for their stock and Berks stock in American was to be can The plaintiffs Grace, et al. were m ty stockholders of American. Plai Leventritt Lewittes & Bender ("L were their counsel. In addition to shire and American the other defe in this action are Daniel K. L

1. Section 17 of the Investment Company Act of 1940, 15 U.S.C. § 80a–17, provides in pertinent part:

(a) It shall be unlawful for any affiliated person or promoter of or principal underwriter for a registered investment company (other than a company of the character described in Section 80a–12(d)(3)(A) and (B) of this title), or any affiliated person of such a person, promoter, or principal underwriter, acting as principal—

(1) knowingly to sell any security or other property to such registered company or to any company controlled by such registered company, unless such sale involves solely (A) securities of which the buyer is the issuer, (B) securities of which the seller is the issuer and which are part of a general offering to the holders of a class of its securities, or (C) securities deposited with the trustee of a unit investment trust or periodic payment plan by the depositor thereof;

(2) knowingly to purchase from such registered company, or from any company controlled by such registered company, any security or other property (except securities of which the seller is the issuer) or

(3) to borrow money or other p from such registered company or fr company controlled by such reg company (unless the borrower i trolled by the lender) except as pe in section 80a-21(b) of this title.

(b) Notwithstanding subsection this section, any person may file w Commission an application for an exempting a proposed transaction applicant from one or more provisi said subsection. The Commission grant such application and issue su der of exemption if evidence esta that—

(1) the terms of the proposed t tion, including the consideration to or received, are reasonable and fair not involve overreaching on the p any person concerned;

(2) the proposed transaction is ent with the policy of each registe vestment company concerned, as rec its registration statement and report under this subchapter; and

(3) the proposed transaction is ent with the general purposes of thi chapter.

(Ludwig) the sole stockholder of Berkshire and Trude Weininger, Premier Investing Corporation and Robert Korsen who were or are, other minority stockholders of American.[2]

The SEC Proceeding

Berkshire filed its 17(b) application on July 31, 1967, proposing a short form merger of American into Berkshire pursuant to the then § 14:12-10 of the New Jersey General Corporation Law which was concededly applicable and permitted a New Jersey corporation owning 90% or more of a New Jersey subsidiary to merge the subsidiary into the parent by resolution of the parent's board of directors setting forth the terms of the merger. Minority stockholders could accept the price fixed in the resolution or demand an appraisal of their stock. Berkshire estimated the net value of American at about $53 million and proposed to offer $275 per share to American minority stockholders.

The parties to the SEC proceeding were Berkshire and the SEC's Division of Corporate Regulation (Rule 9(a), SEC Rules of Practice, 17 C.F.R. § 201.9(a)). The SEC on October 25, 1967 directed a hearing on notice to all interested parties. Grace and the other plaintiffs thereupon retained LLB who appeared for them after leave to participate had been granted pursuant to Rule 9(c), 17 C.F.R. § 201.9(c). Evidentiary hearings on Berkshire's application were conducted before a hearing examiner of the SEC from January 4th to June 7th, 1968, totalling about 50 hearing days. Counsel for the SEC's Division of Corporate Regulation also appeared. Seventeen witnesses testified, 550 exhibits were introduced and a 7500 page transcript of the hearing was compiled. At the end of the hearings the parties agreed pursuant to Rules 8(b) and (c), 17 C.F.R. § 201.8(b) and (c), to waive an initial decision by the hearing examiner and to permit the SEC staff to assist the Commission in the preparation of its decision. A hearing before the full Commission was held on November 12, 1968. Prior to any decision by the Commission, Berkshire advised the SEC that a sale of certain property owned by American might have an impact on the valuation of the American stock. Berkshire thereafter applied for and was granted on June 12, 1969 a re-opening of the proceedings to adduce additional evidence. After two days of hearings (August 4 and 11, 1969) a settlement proposal of Berkshire was rejected by LLB and Berkshire sought leave to withdraw its 17(b) application. The SEC on November 28th, 1969 allowed the withdrawal and denied LLB's claim for a fee to be paid by American or Berkshire, without prejudice to any other legal remedy which the plaintiffs might pursue, since the agency lacked jurisdiction to award counsel fees. This action set the stage for the proceeding below.

The Court Proceedings

On March 20, 1970 plaintiffs commenced an action in the United States District Court, Southern District of New York, seeking attorney's fees and expenses against the defendants arising out of the SEC proceeding. In essence, LLB claims that although Berkshire initially offered only $275 per share as the fair and reasonable value of American shares, primarily due to the services of LLB Berkshire successively raised its offer to $375 per share, $575 per share and eventually $650 per share or more than double the initial offer. American's net value was thus considered to be $126 million instead of the $53 million initially estimated by Berkshire.

Plaintiffs allege that Ludwig and Berkshire, as controlling shareholders, owed a fiduciary obligation to American and its minority shareholders to propose

2. American had 194,177 shares outstanding. Berkshire owned 91% or 176,719 shares. Of the remaining 9% or 17,558 shares, the plaintiff shareholders owned 4,830; defendant Korsen owned 825 and defendants Weininger and Premier Investing Corporation had owned 6,150. The balance, 5,653 shares, were widely held.

the merger on fair and reasonable terms. They claim that these defendants breached that obligation, committed an oppressive fraud against American and its minority shareholders and violated sections 17(a), (b) and 34(b) of the Investment Company Act (15 U.S.C. §§ 80a-17(a), (b) and 80a-33(b)) and sections 10, 14(e) and 27 of the Securities Exchange Act of 1934 (15 U.S.C. §§ 78j, 78n(e) and 78aa) as well as Rule 10b-5 (17 C.F.R. § 240.10b-5) by submitting the merger plan and application, supported by fraudulent misrepresentations, to the SEC.

LLB further claims that through its efforts the plan of Ludwig, Berkshire and American to defraud the American minority stockholder plaintiffs was thwarted and the added value of the American shares has been preserved to American and its stockholders. LLB seeks judgment against Ludwig or alternatively Berkshire or alternatively American for a fair and reasonable attorney's fee of ten million dollars (LLB would reimburse plaintiff stockholders' legal fees of $154,314 already paid to LLB). In the alternative, on the assumption that there was no corporate benefit to American, then Ludwig, Berkshire or American should pay LLB attorney's fees in the sum of $2,418,262 which is alleged to represent the benefit conferred upon the minority shareholders (excluding plaintiff shareholders) plus attorney's fees paid by plaintiffs to LLB. In the alternative, these amounts would be paid proportionately by the defendant shareholders of American. As a last alternative plaintiffs demanded "[t]hat the appropriate combination of defendants be adjudged liable to make appropriate payments quantum meruit to LLB and the appropriate combination of the above, excluding the [defer shareholders of American], make a priate reimbursement to plaintiff s holders of fees paid or payable to L Finally, Grace seeks reimbursemer expenses in the sum of $54,911.92 Ludwig or in the alternative Berks

Discovery proceedings were condu seven witnesses were deposed and s of exhibits were introduced. De ants American, Berkshire and Lu moved for judgment on the pleading cause of the legal insufficiency of complaint; the remaining defenc moved for dismissal or summary j ment. The plaintiffs moved for sur ry judgment with supporting paper cluding a 40 page affidavit of which incorporated the 7500 page hearing transcript, as well as the e its and briefs before the SEC, plus depositions and exhibits in the cas low. The motions were argued on J ary 10, 1973 before the Hon. Whi Knapp, District Judge. Judge K announced that the only issue he w decide was whether the complaint s a cause of action. He assumed the t of the facts alleged in the complaint the supporting papers and then missed the complaint without any fo opinion.[3]

Jurisdiction

An initial and vexing question he finding a basis for the jurisdictio the federal court. The defendant m ity stockholders urge that since the denied LLB's application for a fee, exclusive remedy was an appeal to court which would preclude a colla proceeding in the district court chal ing the agency's ruling. (Securities change Act, § 25(a), 15 U.S.C 78y(a); Investment Company Ac

1. Judge Knapp stated below "no one is interested in my views on this subject but is interested in getting to the Court of Appeals. . . . I don't see anything further to be gained by discussion here or by my writing an opinion. The less I say the quicker you can get before the Court of Appeals." A similar reticence was expressed by the SEC on July 26, 1973 which declined t an *amicus* brief expressing its opinion the propriety of a District Court award fee in the circumstances of this case. sel for all parties have however been ous in supplying this court with ext briefs on appeal.

43(a), 15 U.S.C. § 80a–42(a)). The difficulty with this position is that the SEC simply held that it had no statutory authority to grant a fee and further held that its denial on jurisdictional grounds was without prejudice to LLB's "taking legal action to pursue any remedy they may have in this respect." The present action does not attack the determination that the SEC has no jurisdiction to award a fee but rather seeks a fee to be awarded by the court. There is therefore no res judicata problem here and no collateral attack. The question is whether the district court as a court of equity should award a fee to prevent an unjust enrichment. That question in our view is here litigable.

[1] In essence, the complaint here charges that Berkshire and Ludwig, in proposing the "fair and reasonable" price of $275 per share for American stock in the application to the SEC for a 17(b) exemption, were engaged in a fraudulent scheme to freeze out the public stockholders and to eliminate American as an independent entity. Since we must accept the allegations of the complaint as true on this appeal (Gardner v. Toilet Goods Ass'n, 387 U.S. 167, 172, 87 S.Ct. 1526, 18 L.Ed.2d 704 (1967)), it would appear that the illicit behavior charged is encompassed within the substantive sections of the Investment Company Act, and of the Securities Exchange Act relied upon in the complaint. See Saylor v. Lindsley, 456 F.2d 896, 903–904 (2d Cir. 1972); cf. Entel v. Allen, 270 F.Supp. 60 (S.D.N.Y.1967). However, the jurisdictional sections (section 44 of the Investment Company Act, 15 U.S.C. § 80a–43, and section 27 of the Securities Exchange Act, 15 U.S.C. § 78aa) specify that federal courts shall have jurisdiction only of "violations" of these statutes and actions in equity and at law brought to enforce any "liability or duty" created by the statute or the rules promulgated thereunder. The minority stockholder defendants urge that they have committed no violations of the statutes involved and have no liabilities or duties under such statutes and therefore there is no jurisdiction here as to them. Indeed the complaint urges not that they have made any deceptive statements or participated in any fraudulent schemes but were rather the intended victims. This argument would be persuasive except that the plaintiffs also urge that the federal court has jurisdiction under 28 U.S.C. § 1331 which grants jurisdiction where the amount in controversy exceeds $10,000 and "arises under the Constitution, laws or treaties of the United States." We think that this action for fees and expenses does arise under the stated substantive sections of the Investment Company Act and Securities Exchange Act. Even though the minority stockholder defendants did not violate the sections, it is alleged that they benefitted from the LLB representation. We rely on Judge Friendly's *en banc* opinion in Gilson v. Chock Full O'Nuts Corp., 331 F.2d 107 (2d Cir. 1964) where an attorney had found a claim for recovery of "short swing" profits under § 16(b) of the 1934 Act, 15 U.S.C. § 78p(b), which the corporation at his urging then successfully pursued. We found that an action to recover an attorney's fee for this service to the corporation was a remedial incident to the § 16(b) action and was properly brought in the federal court. The corporation there was not in violation of the Securities laws any more than the minority stockholders here.[4] What we have held with respect to the section 1331 jurisdiction is of course equally applicable to American and *a fortiori* to Ludwig and Berkshire who are accused of substantive violations of the Acts in question in the complaint.

4. It is noteworthy that the *Gilson* litigation was originally commenced in the state courts, but was removed to the federal district court on the express ground that the claim for attorney's fees was one arising under the laws of the United States, specifically section 16(b) of the Securities Exchange Act, 15 U.S.C. § 78p(b). Gilson v. Chock Full O'Nuts Corp., 326 F.2d 246, 247 (2d Cir. 1964).

The Merits

[2-4] In American jurisprudence the general rule is that a successful litigant is not permitted to recover his attorney's fees as damages or as reimbursable costs. Fleischmann Distilling Corp. v. Maier Brewing Co., 386 U.S. 714, 717-720, 87 S.Ct. 1404, 18 L.Ed.2d 475 (1967); Day v. Woodworth, 54 U.S. (13 How.) 362, 371-375, 14 L.Ed. 181 (1852); Arcambel v. Wiseman, 3 U.S. (3 Dall.) 306, 1 L.Ed. 613 (1796).[5] However, it is also established that in special circumstances a court of equity does have the inherent power to reimburse a successful suitor for the costs of litigation, including his attorney's fees. Sprague v. Ticonic National Bank, 307 U.S. 161, 166, 59 S.Ct. 777, 83 L.Ed. 1184 (1939). In J. I. Case Co. v. Borak, 377 U.S. 426, 84 S.Ct. 1555, 12 L.Ed.2d 423 (1964), the Supreme Court emphasized that the private enforcement of the Securities laws as a supplement to SEC action, was highly desirable. It was not surprising therefore that in Mills v. Electric Auto-Lite Co., 396 U.S. 375, 391, 90 S.Ct. 616, 24 L.Ed.2d 593 (1970) the Court gave its approbation to an award of attorney's fees to successful champions who in private litigation had vindicated the policy of the Securities laws. However, the Court found that there were "special circumstances" present which justified the award. We find no such circumstances here; we find no precedent for such an award here and indeed find considerations which would strongly militate against exercising discretion in favor of the plaintiffs

At the heart of the doctrine favo the award of counsel fees in secur cases is the need to encourage the lance of private attorneys genera provide corporate therapy protectin public investor who might otherwis victimized. See Rosenblatt v. North Airlines, Inc., 435 F.2d 1121, 1124 Cir. 1970). Thus in *Borak* the C commented upon the practical inab of the SEC to thoroughly and indep ently examine the veracity of facts out in proxy materials which, excep private litigant scrutiny, would be u tected until after a merger had beer complished. J. I. Case Co. v. Borak *pra*, 377 U.S. at 432-433, 84 S.Ct. Professor Cary has noted in referen proxy statements and written proxy liciting material: "The SEC does purport to pass upon the merits or derwrite the accuracy or adequacy o statements made." W. Cary, Corp tions 306 (4th ed. 1969). The need private enforcement continues and i cented as the filings burgeon.[6]

The same policy underlies the hold of this court in leading cases such Smolowe v. Delendo Corp., 136 F.2d (2d Cir.), cert. denied, 320 U.S. 751 S.Ct. 56, 88 L.Ed. 446 (1943), Gilso Chock Full O'Nuts Corp., 331 F.2d (2d Cir. 1964) (*en banc*), and Bla Rayette-Faberge, Inc., 389 F.2d 469 Cir. 1968), which permitted the reco of attorney's fees where a derivative tion had been brought to recover o

5. In colonial America, most courts adopted the English practice of awarding attorney's fees to the successful party in actions at law. (C. McCormick, Damages 235 (1935)). Explanations as to why this practice was soon abandoned include statutory provisions granting attorneys fixed amounts which eventually lost all relation to actual costs (Ehrenzweig, Reimbursement of Counsel Fees and the Great Society, 54 Cal.L.Rev. 792, 798-99 (1966)), the distrust the colonists felt toward the legal profession (Goodhart, Costs, 38 Yale L.J. 849, 873 (1929)), and the individualistic spirit of the frontier society which viewed lawyers as an unnecessary luxury. (Note, Attorney's Fees: Where Shall the Ultimate Burden Lie Vand.L.Rev. 1216, 1220 (1967)).

6. In *Borak* the Court pointed to the number of proxy statements annually with the SEC (then over 2000) and pressures of time under which the s works in reviewing proxy materials. fiscal year 1969 (the year in question the Commission reported that some proxy statements in final form were vis-a-vis some 249 applications for under the Investment Company Act su ted in that year. SEC, 35th Annual Re 1969, at 46, 133.

instigate the recovery of insider short swing profits under section 16(b) which the corporation had failed or refused to bring on its own behalf. As we pointed out in *Smolowe*, "the possibility of recovering attorney's fees will provide the sole stimulus for the enforcement of § 16(b) . . ." 136 F.2d at 241.

We find no such "special circumstances" here. The role of the SEC in the case at hand was markedly distinguishable. The statute here did not envisage a simple reporting procedure or the mere submission of written materials for pro forma or perfunctory review. Under 17(a) of the Investment Company Act, the merger of American and Berkshire was prohibited unless application was made under 17(b) for an order of exemption. The Commission could only issue such an order if *evidence* established that the consideration to be paid was reasonable and fair and did not involve overreaching, and was consistent with the policy of the investment company and the Act. The SEC called for a hearing before a hearing examiner; extensive hearings were held with the SEC's Division of Corporate Regulation represented by counsel throughout.[7] Eventually, the 17(b) application was withdrawn by Berkshire. In this proceeding LLB entered its appearance on behalf of the Grace stockholders who had over a $3,800,000 interest and who had paid LLB some $154,314 in fees and expenses. In view of the direct and substantial interest of the Grace stockholders, LLB's representation was not stimulated solely by the expectation of fees from those who had not retained them. (See *Smolowe*, *supra*). Inasmuch as Berkshire submitted the application for exemption to the Agency charged with protection of the public investors and extensive proceedings were held, there is no parallel here to cases where SEC scrutiny either has been avoided or in the nature of things its function is ministerial or casual.

LLB takes the position however that it pulled the "laboring oar" in the SEC proceedings and that primarily through its efforts Berkshire continuously increased its offer to the public shareholders. In the posture this case reaches us, these allegations must be accepted as true. We cannot accept, however, the premise that *but for* LLB's intervention the SEC would have approved as "fair and reasonable" the initial offer of Berkshire. If LLB had never appeared how can we properly assume that the SEC would have been so totally supine or so derelict as to give its approval to a price which plaintiffs urge was not merely unconscionably low but was in fact the product of a deception and fraud practiced by Berkshire and Ludwig? The record before us does not permit this inference, and in his letter announcing the Commission's refusal to submit an *amicus* brief, the SEC's General Counsel states: "It is by no means clear to the Commission that but for plaintiffs' intervention in the administrative proceeding the Commission and its then-Division of Corporate Regulation would have sanctioned a violation of the Investment Company Act, and since the application was withdrawn no finding concerning the proposed transaction was made."

7. This distinguishes Honda v. Mitchell, 136 U.S.App.D.C. 22, 419 F.2d 324 (D.C.Cir. 1969), relied upon by plaintiffs. The Attorney General, as successor to the Alien Property Custodian, sponsored hearings to determine the value of yen certificates held by American depositors of a Japanese bank whose assets had been seized during the war. While it is unquestioned that the Attorney General was required to deal "equitably" with the depositors' claims, his position was adverse to the claimants' who demanded that the certificates be redeemed at the pre-war conversion rate, rather than the lower post-war rate he proposed. Clearly the award of counsel fees in that situation is no precedent for plaintiffs' instant claim, for the depositors' interests were not impartially represented by any Government agency. Furthermore, the claimants in *Honda*, unlike the defendants here, actually retained the legal counsel whose prosecution of their claims led in substantial part to the recovery out of which his fee was paid.

The complaint here does not allege that "but for" the LLB intervention the SEC would have granted the application for an exemption based on the initial offer by Berkshire. Appellant relies on the colloquy between Judge Knapp and counsel below in which he stated that he assumed that the SEC had done nothing and in fact had acted "horrendously" (even LLB recoiled from this characterization of the SEC performance). We cannot consider this comment as a finding of fact but only as an assumption not supported by any reference to the record. In re Rosen, 66 F.Supp. 174, 179 (D.N.J.), aff'd, 157 F.2d 997 (3rd Cir. 1946), cert. denied, 330 U.S. 835, 67 S.Ct. 972, 91 L.Ed. 1282 (1947). The motion here was for judgment on the pleadings and even as expanded by the affidavit we do not find warrant for the assumption.

Had the SEC granted the exemption and the initial $275 offer been approved and had LLB then successfully appeared in a derivative action on behalf of the public stockholders, we would have a decidedly different situation. The failure of the SEC to act properly would have been established. Saylor v. Lindsley, *supra*, 456 F.2d at 902–903; Entel v. Allen, *supra;* cf. Thomas v. Honeybrook Mines, Inc., 428 F.2d 981 (3d Cir. 1970), cert. denied, 401 U.S. 911, 91 S.Ct. 874, 27 L.Ed.2d 809 (1971); Powell v. Pennsylvania R.R., 166 F.Supp. 448 (E.D.Pa. 1958), reversed on other grounds, 267 F.2d 241 (3d Cir. 1959).

Assuming that LLB did pull the "laboring oar" in the proceeding before the SEC, it was in the interest of a substantial minority stockholder and it was the basis for a not insignificant fee. The fact that the SEC permitted admittedly able and persistent counsel to man the oars does not at all establish that the vessel would have otherwise foundered. LLB must then be characterized as a mere volunteer who aids a public body or trust in the performance of their official duties on behalf of a certain class, but who is not entitled to compensation. Edison Light & Power Co. v. Pennsylvania Pub. Util. Comm'n, 34 F.Supp. 939 (E.D.Pa.1940), aff'd on the opinion below, 119 F.2d 779 (3d Cir. 1941); King v. City of Covington, 289 Ky. 695, 160 S.W.2d 13 (1942); City of Englewood v. Allison Land Co., 45 N.J.Super. 538, 133 A.2d 680 (App.Div.1957); In re Katz' Estate, 40 N.J.Super. 103, 122 A.2d 185 (Super.Ct.1956); Peoples-Pittsburgh Trust Co. v. Pittsburgh United Corp., 334 Pa. 107, 5 A.2d 890 (1939). See Restatement of Restitution § 115, comment *a*, at 482 (1937).

Although we find no "special circumstances" here which would justify an award of counsel fees we should further state that the equitable basis in any event for such an award is the prevention of unjust enrichment. Mills v. Electric Auto-Lite Co., *supra*, 396 U.S. at 392, 90 S.Ct. 616; Fleischmann Distilling Corp. v. Maier Brewing Co., *supra*, 386 U.S. at 719, 87 S.Ct. 1404. The plaintiff at his own expense has conferred a benefit upon the defendant which justice demands he recompense. Restatement of Restitution § 1 (1937). We cannot agree that American or its principal shareholder, Berkshire (controlled by Ludwig), has been enriched by Grace or LLB. In sum, the complaint urges that Ludwig who controlled Berkshire and in turn American, knew full well the value of the American shares but was bent upon fleecing the public minority shareholders. No matter what transpired before the SEC the intrinsic value of American would be the same in so far as Berkshire and Ludwig were concerned. The merger was aborted and the theory of the complaint is that they have not been enriched but rather deprived by the intervention of plaintiffs. The only possible benefit could be to the minority stockholders who would have received less than half the true value of their holdings. The only other benefit alleged is that American's corporate identity was preserved. Realistically, however, since the merger was never effectuated American still remains with 91% of its shares in the hands of Berkshire with Ludwig still at

the helm. Conceptually the corporation is intact but the Augean stables, if indeed they be, remained uncleansed. We therefore see no merit to the claim that Berkshire or Ludwig should indemnify American because of its debt to the plaintiffs who have realistically conferred no benefit at all upon American.

We do not ignore the contention that Ludwig and Berkshire are directly responsible to the plaintiffs on the theory that a court may award attorney's fees in favor of a party who is forced to litigate by reason of the vexatious, wanton conduct of a defendant who brings an unfounded action or presents an unfounded defense. See Stolberg v. Board of Trustees, 474 F.2d 485 (2d Cir. 1973) and Kahan v. Rosenstiel, 424 F.2d 161 (3d Cir.), cert. denied, 398 U.S. 950, 90 S.Ct. 1870, 26 L.Ed.2d 290 (1970). Judge Mansfield's recent opinion in *Stolberg* reviews the unusual circumstances which authorize the award of counsel fees. In that case, he emphasized that suit was compelled by the defendant's recalcitrant conduct, 474 F.2d at 490. As we have pointed out, the administrative proceeding here was prompted by the statute. The appearance of plaintiffs was compelled by their substantial interest in the price to be fixed for the stock. The extensive participation of LLB was voluntary and, as we have already noted, we cannot assume that the SEC would have failed to act without it. The fraud charged was not for the purpose of abusing process and forcing unnecessary litigation but to freeze out the public stockholders.

[5] We are left then with the claim that the plaintiffs' intervention enriched the minority stockholders and therefore a *quantum meruit* recovery is authorized. In addition to the grounds already set forth, we find in any event no precedent for a recovery on this basis. We agree with appellant that its failure to establish a fund or to appear for a class does not automatically bar a recovery. The fact that minority stockholders did not retain or expressly rejected LLB's representation is not necessarily fatal. See Sprague v. Ticonic National Bank, 307 U.S. 161, 59 S.Ct. 777, 83 L.Ed. 1184 (1939). However, in the cases where the activity of counsel has produced no fund, it has at least resulted in either the establishment of a principle of law which necessarily established a recovery for those who allegedly benefitted or at least contributed to general corporate therapeutics by disclosing a fraud that otherwise would have gone undetected. This plaintiffs have failed to establish. In *Ticonic, supra*, a private litigant established her right to funds which she had deposited in a bankrupt institution. The court stated:

> In her main suit the petitioner neither avowed herself to be the representative of a class nor did she automatically establish a fund in which others could participate. But in view of the consequences of *stare decisis*, the petitioner by establishing her claim necessarily established the claims of fourteen other trusts pertaining to the same bonds. 307 U.S. at 166, 59 S.Ct. at 780.

Since the SEC proceeding was terminated here by withdrawal of the application for exemption, LLB established no violation of the Securities acts and created no fund for the benefit of the minority stockholders. At best, LLB succeeded in prodding Berkshire-Ludwig over a two year period from an offer of $275 to $650 per share. But the offer was never accepted and no valuation binding upon the offeror was ever established. Thus, in this case, the Weininger appellees sold their American stock to Berkshire at the $275 per share offer in October, 1967 with the understanding that if any other shareholder within a year received a higher price or if the SEC ordered a higher price in the 17(b) proceeding, they would receive the difference. Since neither eventuality occurred they were not entitled to additional sums and Berkshire instead offered to rescind the agreement. Weininger then commenced an action in February, 1970 (Weininger v. National Bulk Carriers, 70 Civ. 610 (S.D.N.Y.)) to recover damages under the federal Securities laws.

In 1972, after extensive discovery, the action was settled at less than $635 per share with Weininger expending some $108,500 in counsel fees plus additional amounts for disbursements. LLB had not established any statutory violation which automatically inured to their benefit.

The offer by Berkshire-Ludwig obviously failed to establish any market value under the circumstances and to now assess additional counsel fees upon unwilling minority stockholders who were forced to lengthy and expensive litigation to achieve any benefit, does not particularly appeal to this court of equity.

In conclusion, we find not only that there is no precedent for the award here sought but in fact that there are policy considerations against it. Aside from the lack of special circumstances calling for the intervention of a private attorney general as well as the difficulty of assessing the value of the putative benefit here, we would face the impossible task of attempting to measure the value of the service of the intervenor. A precedent here would encourage intervention in comparable cases not only before the SEC but other agencies as well. The competition and maneuvering among counsel to assume the lead role would not only be disruptive of administrative procedures but might very well encourage agency inaction. The SEC was here charged with a responsibility and it presumably has the expertise to make the assessment required by the statute. The introduction of additional cooks might not only spoil the broth but paralyze the chef. See Casey v. Woodruff, 49 N.Y.S.2d 625, 648 (Sup.Ct. 1944). A district court would be hard put to determine the value of the contributions of each in a subsequent action far removed from the agency proceeding. If in fact the role of the SEC in these cases is or becomes perfunctory then the statute might be amended to provide for legal fees to be fixed by the agency which has conducted the proceeding and which is in a much better position to estimate the value of the intervenor's contribution. As Judge Kaufman pointed out in Greene County Planning Board v. FPC, 455 F.2d 412, 427 (2d Cir.), cert. denied, 409 U.S. 849, 93 S.Ct. 56, 34 L.Ed.2d 90 (1972), in somewhat comparable circumstances:

> Fully mindful that petitioners invoke our equitable powers, we cannot ignore parallel developments in this rapidly changing area of administrative law. As recently as December 7, 1971, the Administrative Conference of the United States refused to adopt a recommendation which would have endorsed the principle of reimbursing the legal expenses incurred by intervenors in administrative proceedings . . . . Recommendation 28, Public Participation in Administrative Hearings § D, adopted December 7, 1971. Without a showing of compelling need, it would be premature for us to inject the federal courts into this area of administrative discretion, perhaps foreclosing more flexible approaches through agency action or rules.

For those reasons we affirm the judgment below dismissing the complaint for failure to state a cause of action.

APPENDIX B

Orders of Court of Appeals Denying Petition for Rehearing, Dated and Entered November 14, 1973.

UNITED STATES COURT OF APPEALS

SECOND CIRCUIT

At a stated term of the United States Court of Appeals in and for the Second Circuit held at the United States Court House, in the City of New York on the fourteenth day of November one thousand nine hundred and seventy-three.

Docket No. 73-1212

Present:

HON. PAUL R. HAYS

HON. WALTER R. MANSFIELD

HON. WILLIAM H. MULLIGAN,

Circuit Judges.

[SAME TITLE]

A petition for a rehearing having been filed herein by counsel for the appellants,

Upon consideration thereof, it is

Ordered that said petition be and it hereby is denied.

A. DANIEL FUSARO
Clerk

Orders of Court of Appeals Denying Petition for Rehearing, Dated and Entered November 14, 1973.

UNITED STATES COURT OF APPEALS

SECOND CIRCUIT

At a Stated Term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Court House, in the City of New York, on the Fourteenth day of November, one thousand nine hundred and seventy-three.

[SAME TITLE]

A petition for a rehearing containing a suggestion that the action be reheard in banc having been filed herein by counsel for the appellants, and no active judge or judge who was a member of the panel having requested that a vote be taken on said suggestion,

Upon consideration thereof, it is

Ordered that said petition be and it hereby is DENIED.

IRVING R. KAUFMAN
Chief Judge

IRVING R. KAUFMAN

APPENDIX C

District Court's Statement in Open Court on January 10, 1973 of Grounds for Granting Motion.

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

[SAME TITLE]

January 10, 1973,
9:30 A.M.

Before: HON. WHITMAN KNAPP, District Judge.

The Court: I am just saying that basically no one is interested in my views on this subject but is interested in getting to the Court of Appeals. I think the record that we have made here clearly puts the issue before the Court of Appeals. I don't see anything further to be gained by discussion here or by my writing an opinion. The less I say the quicker you can get before the Court of Appeals.

It is my view as indicated, and Judge Feinberg can very quickly set my right if I am wrong, that the section of the Blau case that I called attention to, page 473 beginning with paragraph 1, clearly indicates the Court of Appeals similarly held and I accordingly grant the motion on the ground that the SEC staff had the statutory duty to do what plaintiff alleges he did and it is immaterial whether they did it or not, the plaintiff is not entitled to a fee.

APPENDIX D

Judgment of District Court Dismissing Complaint, Dated and Entered January 11, 1973.

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

[SAME TITLE]

Defendants having moved the Court pursuant to Rules 12(c) and 56(b) of the Federal Rules of Civil Procedure to dismiss the complaint, and the said motion having come on to be heard before the Honorable Whitman Knapp, United States District Judge, and the Court thereafter on January 10, 1973, having handed down its memorandum endorsed granting the said motion for the reasons stated in open Court, it is,

ORDERED, ADJUDGED AND DECREED: That the defendants, Daniel K. Ludwig, Berkshire Industries, Inc., American-Hawaiian Steamship Company, Trude Weininger, Premier Investing Corporation and Robert Korsen, have judgment against the plaintiffs, Oliver R. Grace, The Green Fund, Inc., S. William Green, Evelyn Green and Cynthia Colin, as Executors of The Estate of Louis A. Green, Deceased, Evelyn Green and Elbridge Smith, Individually and as Stockhoders of American-Hawaiian Steamship Company in Behalf of Themselves and of said Corporation, and Leventritt, Lewittes & Bender, dismissing the Complaint.

Dated: New York, N. Y.
January 11, 1973

JOHN LIVINGSTON
Clerk

APPENDIX E

Four Communications Between the Court of Appeals and the SEC.

(1)

UNITED STATES COURT OF APPEALS
SECOND CIRCUIT
New York, N. Y. 10007

Chambers of
WILLIAM HUGHES MULLIGAN
Circuit Judge
1 Federal Plaza

June 26, 1973

Walter North, Esq.
Acting General Counsel
Securities & Exchange Commission
500 North Capitol Street
Washington, D.C. 20549

Re: Oliver R. Grace et al
v. Daniel K. Ludwig et al, Docket # 73-1212

Dear Mr. North:

Earlier this month this court heard argument on appeal in the above entitled matter. I enclose a copy of the brief and reply brief of the appellants and the briefs of the appellees, as well as the two volume appendix.

This case so far as counsel has ascertained presents a question of first impression—the right of counsel representing minority stockholders before the Securities and Exchange Commission in a proceeding under Section 17(a) and (b) of the Investment Company Act, to a fee to be assessed against the corporation or other stockholder for

the benefits accruing due to services rendered in the proceeding. The court would be grateful for a brief expressing the views of the Commission on this question as well as the other points raised in the briefs, including the role of the SEC in this proceeding and similar cases.

We are not unmindful of the burdens on the Commission but we would appreciate it if the brief could be filed by July 27, 1973. A copy should be served on: Leventritt Lewittes & Bender, 135 East 42nd Street, New York, New York 10017 (attorneys for plaintiffs-appellants); Pomerantz Levy Haudek & Block, 295 Madison Avenue, New York, New York; Morrison, Paul, Stillman & Beiley, 110 East 59th Street, New York, N.Y. 10022; Stroock & Stroock & Lavan, 61 Broadway, New York, N.Y. 10006 (attorneys for defendants-appellees.)

The brief may be filed in typewritten or xerox form. At least four copies should be filed for use of the court.

Please advise me at your early convenience whether the Commission will file a brief.

Sincerely,

WILLIAM H. MULLIGAN
William Hughes Mulligan
United States Circuit Judge

cc: Leventritt Lewittes & Bender
Pomerantz Levy Haudek & Block
Morrison, Paul, Stillman & Beiley
Stroock & Stroock & Lavan
William Moran, Regional Administrator, SEC

Four Communications Between the Court of Appeals and the SEC.

(2)

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

OFFICE OF THE
GENERAL COUNSEL

July 26, 1973

Honorable William Hughes Mulligan
Judge, United States Court of Appeals
for the Second Circuit
Foley Square
New York, New York 10007

Re: *Grace* v. *Ludwig* (Docket No. 73-1212)

Dear Judge Mulligan:

The Commission has determined that it would not be appropriate for it to file a brief in this case. I sincerely regret that we are informing you of this decision almost on the date that you requested a brief be filed, if one were to be submitted. However, the matter required the most careful consideration at the staff level, as well as by the Commission itself.

The Commission is of the view that it was without jurisdiction to award counsel fees in the proceeding before it, and the Commission so stated in its opinion terminating the administrative proceeding upon withdrawal of Berkshire's application under Section 17(b) of the Investment Company Act (Ap. 138). While a court of equity may, without specific statutory authority, grant reimbursement for counsel fees as "part of the original authority of the chancellor to do equity in a particular situation,"[1] an ad-

[1] *Mills* v. *Electric Auto-Lite Co.*, 396 U.S. 375, 393 (1970), quoting *Sprague* v. *Ticonic National Bank*, 307 U.S. 161, 166 (1939).

ministrative agency must look to the legislature that created it as the exclusive source of its power. The Investment Company Act of 1940 contains no such grant of power, either explicitly or by reasonable implication. Whether a federal district court may award counsel fees for participation in a proceeding before a federal regulatory agency, where the fee award is the only relief sought in the court suit, is, the Commission believes, a question of the jurisdiction of federal courts and not one within the Commission's expertise.

In addition, the Commission notes that the plaintiffs have devoted the major portion of their briefs to an attack upon the Commission's handling of the administrative proceeding. It is by no means clear to the Commission that but for plaintiffs' intervention in the administrative proceeding the Commission and its then-Division of Corporate Regulation would have sanctioned a violation of the Investment Company Act, and since the application was withdrawn no finding concerning the proposed transaction was made.

Under separate cover I am returning to the Clerk of the Court the briefs and appendix which you sent to Mr. North.

The Commission sincerely appreciates the Court's invitation to express its views in this proceeding.

Yours very truly,

LAWRENCE E. NERHEIM
Lawrence E. Nerheim
General Counsel

cc: A. Daniel Fusaro, Esq.
Leventritt, Lewittes & Bender
Pomerantz, Levy, Haudek & Block
Morrison, Paul, Stillman & Beiley
Stroock & Stroock & Lavan

Four Communications Between the Court of Appeals and the SEC.

(3)

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

OFFICE OF THE
GENERAL COUNSEL

October 18, 1973

Honorable Paul Hays
Honorable Walter Mansfield
Honorable William H. Mulligan
Judges, United States Court of Appeals
for the Second Circuit
United States Courthouse
Foley Square
New York, New York 10007

Re: *Grace* v. *Ludwig* (Docket No. 73-1212)

Dear Judges Hays, Mansfield and Mulligan:

We understand that plaintiffs-appellants in this action have filed a petition for rehearing of the Court's decision of September 12, 1973. As the Court will recall, the Commission, by letter of July 26, 1973, declined to file a brief *amicus curiae* in this appeal. The Commission has also declined the request of Sidney Bender, Esq., plaintiffs' counsel, to file a brief in support of the petition for rehearing. The Commission takes no position with respect to the result reached by the Court in this case. However, there is one aspect of the opinion of the panel which the Commission finds troublesome, and the Commission respectfully requests this opportunity to set forth its views as to that one aspect of the opinion.

The Court cited and discussed a number of reasons for affirming the district court's decision which had dismissed this suit. At the end of the opinion (slip op., 5146), the

Court stated: "We find not only that there is no precedent for the award here sought, but in fact that there are policy considerations against it." The Court continued:

> "A precedent here would encourage intervention in comparable cases not only before the SEC but other agencies as well. The competition and maneuvering among counsel to assume the lead role would not only be disruptive of administrative procedures but might very well encourage agency inaction. . . . The introduction of additional cooks might not only spoil the broth but paralyze the chef." (slip op., 5147).

The Commission respectfully urges the Court to delete from its opinion the paragraph in which the above language appears. The Commission fears that the thrust of the paragraph is to discourage the participation of interested persons in administrative proceedings before the Commission, more precisely, to discourage the participation of minority shareholders in proceedings arising under Section 17(b) of the Investment Company Act of 1940, 15 U.S.C. 80a-17(b). The Commission welcomes the participation of responsible persons in its administrative proceedings. The Commission does not share the Court's fear that "additional cooks might . . . spoil the broth" and is confident that it could deal with "competition and maneuvering among counsel" who are more interested in collecting fees than in securing a just result in the proceedings before the Commission.

The Commission often finds participation by interested persons in administrative proceedings helpful in achieving a just result. Section 40(a) of the Investment Company Act, 15 U.S.C. 80a-39(a), provides that orders of the Commission may not be issued without appropriate notice and

opportunity for hearing. The Commission has promulgated rules governing participation by interested persons in proceedings before it. See Rule 9 of the Commission's Rules of Practice, 17 C.F.R. 201.9.

In applications under Section 17(b) of the Investment Company Act, it is the staff's practice to examine carefully the application and accompanying documents and other materials in the Commission's files that would be relevant to the application. As the Court observes, the Investment Company Act does not envisage "a simple reporting procedure or the mere submission of certain materials for pro forma or perfunctory review." (slip op., at 5140). The staff and the Commission must pass on the merits of the application. However, if there does not appear from a careful examination of the application and other documents anything to indicate that the proposed transaction would be unfair or otherwise not in accordance with the terms of the Investment Company Act, the Commission, in all probability, will not itself set the application for hearing.[1] A notice of the filing of the application, together with a description of the proposed transaction, will be published. The notice will recite that if the Commission does not set the matter for hearing pursuant to the request of an interested person or on its own motion, then the application will be granted without a hearing. If no hearing is ordered, and the application is granted without one, the application will constitute evidence supporting the Commission's favorable action on it. See slip op. at 5140; Investment Company Act of 1940, Section 40(b), 15 U.S.C. 80a-39(b); Investment Company Act of 1940, Rule 0-2(d), 17 C.F.R. 270.0-2(d). However, the evidence supporting the application

[1] In the circumstances of the application that forms the subject of this suit, the Commission did itself set the matter for hearing. See slip op. at 5132.

is of necessity one-sided, and the Commission's staff does not and cannot conduct a full-scale investigation of the merits of applications, except in those relatively rare instances where the application appears to require such.

If an interested person has information tending to show that the proposed transaction does not in fact comply with the statutory standards, it is essential for effectuation of the policies of the Act that that person bring his views to the Commission's attention. We believe that the effect of the paragraph in the Court's opinion beginning at page 5146 could be to discourage the participation of interested persons in Commission proceedings and therefore, in the Section 17(b) context, for example, to deprive the Commission of the knowledge of interested persons other than the applicant. While the Commission adheres to the view that it is without power to condition the withdrawal of a Section 17(b) application upon provisions for the payment of participants' counsel fees,[2] the Commission is not convinced that in all situations it is without authority to condition the grant of an application on the apportionment of fees. For example, where in a Section 17(b) proceeding the Commission finds the proposed transaction to be unfair or otherwise not consistent with statutory standards and where the application is modified so that the transaction is carried out upon terms the Commission finds to be fair, the Commission might condition the grant of a modified application upon payment by the applicant of counsel fees incurred by a participant who had taken a substantial role in bringing the fact of unfairness to the Commission's attention. *Cf., In the Matter of Atlas Corp.,* 39 S.E.C. 437, 461 (1959).

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[2] *In the Matter of Berkshire Industries, Inc.,* Investment Company Act Release No. 5905 (November 28, 1969). This view was reiterated in our letter to the Court of July 26, 1973.

Four Communications Between the Court of Appeals and the SEC.

The "policy considerations" alluded to by the Court at pp. 5146-5147 of its opinion could be read to indicate that, so long as the Commission's role in Section 17(b) proceedings is more than "perfunctory", under no circumstances may a participant be compensated for his counsel fees and expenses. If his is so, then a person with knowledge of facts indicating that a Section 17 application should not be granted will be encouraged to sit out the administrative proceeding and, if the Commission approves the application, to make a collateral attack upon the transaction in district court alleging that the Commission was defrauded. In the collateral action, counsel would probably be entitled to reimbursement of counsel fees, as the Court suggests in its opinion, slip op. at 5142. The net effect, then, would be to by-pass the Commission and to wage the battle of the fairness of the transaction in district court, rather than before the Commission, which is the forum established by Congress for the determination of such questions.

For the foregoing reasons the Commission respectfully urges the Court to delete from its opinion in this case the paragraph beginning at p. 5146 beginning "In conclusion . . ."

Yours very truly,

LAWRENCE E. NERHEIM
LAWRENCE E. NERHEIM
General Counsel

cc: A. Daniel Fusaro, Esq.
Clerk

All Counsel

Four Communications Between the Court of Appeals and the SEC.

(4)

October 29, 1973

Lawrence E. Nerheim, Esq.
General Counsel
Securities and Exchange Commission
Washington, D.C. 20549

Dear Mr. Nerheim:

Re: Grace v. Ludwig (Docket #73-1212)

I have your letter of October 18, 1973 requesting that the court delete a paragraph in the opinion filed in the above entitled matter. I also note that your request has been publicized on the front page of the New York Law Journal of October 25, 1973.

You will recall that on June 26, 1973 a letter was addressed to the Acting General Counsel of the Securities and Exchange Commission requesting that a brief be filed which would express the views of the Commission on the question at issue as well as the "role of the SEC in this proceeding and similar cases." On July 26, 1973, one day before the brief was due, I was advised by you that the Commission did not deem it appropriate to file a brief.

We do not deem it appropriate at this late date to accede to the Commission's request to delete a paragraph of the opinion because of some apprehension that it may possibly discourage participation in some future proceedings. The opinion will not be altered.

Very truly yours,

WM. H. MULLIGAN
William Hughes Mulligan,
United States District Judge

Copies to Counsel

APPENDIX F

Judgment of Court of Appeals Affirming Dismissal of Complaint, Dated and Entered September 12, 1973.

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

At a stated Term of the United Statss Court of Appeals for the Second Circuit, held at the United States Courthouse in the City of New York, on the twelfth day of September, one thousand nine hundred and seventy-three.

Present: HON. PAUL R. HAYS
HON. WALTER R. MANSFIELD
HON. WILLIAM H. MULLIGAN, Circuit Judges.

[SAME TITLE]

This cause came on to be heard on the transcript of record from the United States District Court for the Southern District of New York, and was argued by counsel.

ON CONSIDERATION WHEREOF, it is now hereby ordered, adjudged and decreed that the judgment of said District Court be and it hereby is affirmed with costs to be taxed against the appellants.

A. DANIEL FUSARO
Clerk

By: VINCENT A. CARLIN
Chief Deputy Clerk